VZCZCXRO3796
RR RUEHCD RUEHGD RUEHHO RUEHMC RUEHNG RUEHNL RUEHRD RUEHRS RUEHTM
DE RUEHME #3010/01 2921858
ZNR UUUUU ZZH
R 191858Z OCT 09
FM AMEMBASSY MEXICO
TO RUEHC/SECSTATE WASHDC 8659
INFO RUEHXC/ALL US CONSULATES IN MEXICO COLLECTIVE
RHMFISS/DEPT OF ENERGY WASHINGTON DC
RUEHC/DEPT OF LABOR WASHINGTON DC
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDOC/DEPT OF COMMERCE WASHINGTON DC
RHEHAAA/NSC WASHINGTON DC

UNCLAS SECTION 01 OF 03 MEXICO 003010

SENSITIVE
SIPDIS

STATE FOR WHA/MEX, WHA/EPSC, EEB
NSC FOR RESTREPO, FROMAN
USDOC FOR 4320/ITA/MAC/WH/ONAFTA/GWORD
TREASURY FOR NANCY LEE, IA
ENERGY FOR WARD, LOCKWOOD AND DAVIS

E.O. 12958: N/A
TAGS: ECON EFIN ETRD ENRG ELTN EAIR PGOV PINR SENV
MX
SUBJECT: 2010 GOM BUDGET: OPPOSITION REJECTS AND BUSINESS
SUPPORTS TAX HIKES

REF: MEXICO 2832

¶1. (SBU) Summary. Facing an October 20 deadline to approve the GOM's 2010 proposed revenue bill, PRI leaders, governors, and lawmakers met on October 12 to coordinate a consensus on the budget. According to local press reports, PRI lawmakers revealed that they will reject the GOM's 2% anti-poverty tax proposal and propose to lower the telecommunications tax, increase the deficit to 0.75% (in lieu of the 0.5% proposed by the GOM), and raise the Mexican oil mix benchmark price to US$61 per barrel (instead of US$53.9 set by the GOM). They will formally announce their proposal on October 19. The left-wing PRD is also rejecting the anti-poverty tax and has presented an alternative plan that also proposes a higher oil price, an increase in the deficit, as well as spending cuts. Mexico's leading business consortium, the Consejo Coordinador Empresarial (CCE), supports increases in income and consumption taxes, but demands a lower rate for new investments. End Summary.

PRI

¶2. (U) On October 12, the PRI held a 4-hour meeting to coordinate a formal position on the GOM's economic plan. According to local press reports, PRI lawmakers revealed that they will take the following position, which they will formally announce on October 19.

-- Reject the GOM's 2% anti-poverty tax proposal.
-- Agreed to increase the special tax (IEPS) on beer, tobacco, gambling, the lottery, etc.
-- In lieu of the 4% tax on telecommunications, they will propose an increase of 1.5 and 2%.
-- Agree to increase the income tax (ISR), although they did not specify if it was from 28 to 30% as proposed by the GOM.
-- Agree to raise the tax on cash deposits (IDE) to 3% and lower the floor on taxable deposits to MX$15,000 (from MX$25,000), as proposed by the GOM.
-- Propose to increase the deficit 0.75%, in lieu of the 0.50% proposed by the GOM.
-- Propose to raise the benchmark Mexican oil price to US$61 per barrel, instead of US$53.9 set by the GOM.

3.(U) According to PRI estimates, their proposal would generate MX$375 billion enough to cover the GOM's estimated fiscal gap of MX$374 billion for 2010. The PRI lawmakers

interviewed also said the party agreed to increase the income tax because it would have a larger impact on the middle class, which is mainly the PAN's constituency.

PRD

¶4. (U) The PRD presented an alternative 2010 budget proposal, which proposes an additional MX$550 billion (US$41.77 billion) in revenue. The PRD's proposal estimates that crude oil prices in 2010 would be US$57 per barrel, or US$3.1 higher than the GOM's estimates, which would generate an additional MX$25 billion (MX$1.9 billion) in revenue. The PRD's proposal also contemplates an increase in public debt to 1.5% of GDP, generating an additional MX$180 billion (US$13.67 billion) to be spent on &productive investment and job creation.8 The PRD's plan also proposes MX$100 billion (US$7.6 billion) in cuts to the GOM's running expenses, MX$170 billion (US$12.9 billion) to be generated by eliminating special tax regimes, and MX$75 billion (US$5.7 billion) from a tax on dividends. PRD Chairman Jesus Ortega explained that his party opposed plans for a 2% consumer tax which, he argued, would affect the poor and the middle classes. Furthermore, the PRD proposed that food and medicines remain tax free, and affirmed that the GOM,s plans to increase taxation would extend the economic crisis currently affecting Mexico.

¶5. (U) Meanwhile, the movement led by former presidential candidate Andres Manuel Lopez Obrador is set to present two

bills on austerity in the public sector, which aim to abolish the fiscal privileges of large companies and thus generate an additional 500 billion pesos ($38 billion) in public income. Lopez Obrador explained that his austerity bill proposed a 50% salary cut for top-ranking officials, as well as the elimination of bonuses, major medical expenses, extraordinary payments, and special savings accounts for top-level bureaucrats. Furthermore, the bill would eliminate pensions for former presidents of Mexico, would cut publicity budgets within the public administration by 80%, and would mandate 30% savings in telephone services, consultancy, computers, photocopies, stationery, and other supplies. Lopez Obrador's proposals will be defended by deputies and senators belonging to the Broad Progressive Front (FAP) -- formed by the PRD, the PT, and the Convergence Party.

Private Sector

¶6. (U) As budget negotiations continue, Mexico's leading business consortium, the Consejo Coordinador Empresarial (CCE), said that they are willing to accept the 28% to 30% increase in the income tax (ISR), but only if it is lowered to 25% for new investments or re-investments, which they consider an essential stimulus for the economy. They also want to eliminate exemptions from the VAT and implement a generalized VAT by increasing it from 10% to 15% at the border. The CCE also sent a letter signed by many associations, including the Mexican Banking Association, to lawmakers saying that they were unwilling to pay more taxes if the GOM did not reduce its current expenditures. They complained that while the GOM was increasing taxes to captive taxpayers, it was increasing current expenditures by more than 5% and cutting public investment by 10%. They also called for a reduction in political parties, budgets.

¶7. (U) The business sector continues to be concerned about the GOM's proposed reform to the tax consolidation regime (see reftel). They complain that the changes do not give legal certainty to investors and are an excessive fiscal burden particularly for exporters. According to Hacienda, large companies only paid 1.7% of income tax (rather than the 28%) due to fiscal consolidation and the existing income tax

exemptions. Deputy Secretary of Hacienda Alejandro Werner told lawmakers that the changes proposed in the income tax would generate MX$70 billion, 38% of which is from the proposed changes in fiscal consolidation. Note: All parties have agreed on approving this reform. End Note.

PAN

¶8. (U) Responding to the CCE's complaint on political party transfers, PAN leader and lawmaker Cesar Nava proposed cutting these transfers in half so that political parties could raise a larger share of their resources from private organizations. PAN senators also submitted an initiative to modify the Fiscal Coordination Law, so that states could collect more taxes on their own. The initiative was accompanied by measures to make spending of public resources by the states more transparent.

Recent GOM Actions

¶9. (U) Meanwhile, the GOM has taken other actions outside of the budget/fiscal reform negotiations to accelerate public works projects and improve its fiscal position. On October 1, Calderon announced he would propose legislation that would accelerate plans to build highways and ports and encourage new investment to bolster the economy. The proposal would allow Mexico's pension funds (Afores), to buy stocks outside of indexes and take part in initial public offerings to channel resources to infrastructure projects. Pension funds could also participate in the offering of infrastructure-project trusts on the Mexican stock exchange.

The proposal would cut bureaucratic hurdles to reduce the time it takes to carry out public works projects by 30 percent, Calderon said. He added that it may allow the GOM to announce 61 billion pesos in new projects by the end of 2010, and to increase financing for projects by 125 billion pesos by 2012.

¶6. (U) Also, on October 10, Calderon issued a decree ordering the liquidation of Luz y Fuerza (SEPTEL). Federal Electricity Commission (CFE), Mexico's other state power company, will take over Luz y Fuerza del Centro, the smaller money-losing state power company. According to SEGOB, the financial situation of Luz y Fuerza is unsustainable. If Luz y Fuerza were left to continue, the GOM would have to transfer an estimated 300 billion pesos to the company by ¶2012.

Comment

¶10. Most governors do not want a confrontation with President Calderon, as it could be costly for all parties in the run-up to the 2012 elections. According to the PRI lawmakers interviewed, State of Mexico PRI governor and current presidential front-runner Enrique Pena Nieto was among those who supported the GOM,s 2% anti-poverty tax. He was also against raising the benchmark oil price, because if oil prices declined it would gravely affect states' finances (as it did this year). (Note: States receive over 90% of their resources from the federal government which is determined through a special formula. Oil hedge funds are not shared with the states. End Note.) It would also mean bad news for governors and their candidates who face local elections next year, many of which are PRI-governed states. As the presidential front-runner, it is also in Pena Nieto's interest to take on the more difficult fiscal/tax reforms now, rather than have to deal with a fiscal quandary in 2012. The PRI's counter-proposal achieves fiscal stability mainly

by playing with the oil price assumptions and incurring more debt, but so far there is nothing in their proposal that would generate alternative revenue sources to replace their dependence on oil.

Visit Mexico City's Classified Web Site at http://www.state.sgov.gov/p/wha/mexicocity and the North American Partnership Blog at http://www.intelink.gov/communities/state/nap /

PASCUAL